

(2) *Existing binding contracts.* The section 4958 taxes do not apply to any transaction occurring pursuant to a written contract that was binding on September 13, 1995, and at all times thereafter before the transaction occurs. A written binding contract that is terminable or subject to cancellation by the applicable tax-exempt organization without the disqualified person's consent (including as the result of a breach of contract by the disqualified person) and without substantial penalty to the organization, is no longer treated as a binding contract as of the earliest date that any such termination or cancellation, if made, would be effective. If a binding written contract is materially changed, it is treated as a new contract entered into as of the date the material change is effective. A material change includes an extension or renewal of the contract (other than an extension or renewal that results from the person contracting with the applicable tax-exempt organization unilaterally exercising an option expressly granted by the contract), or a more than incidental change to any payment under the contract.

[T.D. 8978, 67 FR 3083, Jan. 23, 2002]

§ 53.4958-2 Definition of applicable tax-exempt organization.

(a) *Organizations described in section 501(c)(3) or (4) and exempt from tax under section 501(a)*—(1) *In general.* An applicable tax-exempt organization is any organization that, without regard to any excess benefit, would be described in section 501(c)(3) or (4) and exempt from tax under section 501(a). An applicable tax-exempt organization also includes any organization that was described in section 501(c)(3) or (4) and was exempt from tax under section 501(a) at any time during a five-year period ending on the date of an excess benefit transaction (the lookback period).

(2) *Exceptions from definition of applicable tax-exempt organization*—(i) *Private foundation.* A private foundation as defined in section 509(a) is not an applicable tax-exempt organization for section 4958 purposes.

(ii) *Governmental unit or affiliate.* A governmental unit or an affiliate of a

governmental unit is not an applicable tax-exempt organization for section 4958 purposes if it is—

(A) Exempt from (or not subject to) taxation without regard to section 501(a); or

(B) Relieved from filing an annual return pursuant to the authority of § 1.6033-2(g)(6).

(3) *Organizations described in section 501(c)(3).* An organization is described in section 501(c)(3) for purposes of section 4958 only if the organization—

(i) Provides the notice described in section 508; or

(ii) Is described in section 501(c)(3) and specifically is excluded from the requirements of section 508 by that section.

(4) *Organizations described in section 501(c)(4).* An organization is described in section 501(c)(4) for purposes of section 4958 only if the organization—

(i) Has applied for and received recognition from the Internal Revenue Service as an organization described in section 501(c)(4); or

(ii) Has filed an application for recognition under section 501(c)(4) with the Internal Revenue Service, has filed an annual information return as a section 501(c)(4) organization under the Internal Revenue Code or regulations promulgated thereunder, or has otherwise held itself out as being described in section 501(c)(4) and exempt from tax under section 501(a).

(5) *Effect of non-recognition or revocation of exempt status.* An organization is not described in paragraph (a)(3) or (4) of this section during any period covered by a final determination or adjudication that the organization is not exempt from tax under section 501(a) as an organization described in section 501(c)(3) or (4), so long as that determination or adjudication is not based upon participation in inurement or one or more excess benefit transactions. However, the organization may be an applicable tax-exempt organization for that period as a result of the five-year lookback period described in paragraph (a)(1) of this section.

(6) *Examples.* The following examples illustrate the principles of this section, which defines an applicable tax-exempt organization for purposes of section 4958:

Example 1. O is a nonprofit corporation formed under state law. O filed its application for recognition of exemption under section 501(c)(3) within the time prescribed under section 508(a). In its application, O described its plans for purchasing property from some of its directors at prices that would exceed fair market value. After reviewing the application, the IRS determined that because of the proposed property purchase transactions, O failed to establish that it met the requirements for an organization described in section 501(c)(3). Accordingly, the IRS denied O's application. While O's application was pending, O engaged in the purchase transactions described in its application at prices that exceeded the fair market values of the properties. Although these transactions would constitute excess benefit transactions under section 4958, because the IRS never recognized O as an organization described in section 501(c)(3), O was never an applicable tax-exempt organization under section 4958. Therefore, these transactions are not subject to the excise taxes provided in section 4958.

Example 2. O is a nonprofit corporation formed under state law. O files its application for recognition of exemption under section 501(c)(3) within the time prescribed under section 508(a). The IRS issues a favorable determination letter in Year 1 that recognizes O as an organization described in section 501(c)(3). Subsequently, in Year 5 of O's operations, O engages in certain transactions that constitute excess benefit transactions under section 4958 and violate the proscription against inurement under section 501(c)(3) and § 1.501(c)(3)-1(c)(2). The IRS examines the Form 990, "Return of Organization Exempt From Income Tax", that O filed for Year 5. After considering all the relevant facts and circumstances in accordance with § 1.501(c)(3)-1(f), the IRS concludes that O is no longer described in section 501(c)(3) effective in Year 5. The IRS does not examine the Forms 990 that O filed for its first four years of operations and, accordingly, does not revoke O's exempt status for those years. Although O's tax-exempt status is revoked effective in Year 5, under the *lookback* rules in paragraph (a)(1) of this section and § 53.4958-3(a)(1) of this chapter, during the five-year period prior to the excess benefit transactions that occurred in Year 5, O was an applicable tax-exempt organization and O's directors were disqualified persons as to O. Therefore, the transactions between O and its directors during Year 5 are subject to the applicable excise taxes provided in section 4958.

(b) *Special rules*—(1) *Transition rule for lookback period.* In the case of any excess benefit transaction occurring before September 14, 2000, the lookback period described in paragraph (a)(1) of

this section begins on September 14, 1995, and ends on the date of the transaction.

(2) *Certain foreign organizations.* A foreign organization, recognized by the Internal Revenue Service or by treaty, that receives substantially all of its support (other than gross investment income) from sources outside of the United States is not an organization described in section 501(c)(3) or (4) for purposes of section 4958.

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§ 53.4958-3 Definition of disqualified person.

(a) *In general*—(1) *Scope of definition.* Section 4958(f)(1) defines *disqualified person*, with respect to any transaction, as any person who was in a position to exercise substantial influence over the affairs of an applicable tax-exempt organization at any time during the five-year period ending on the date of the transaction (the *lookback period*). Paragraph (b) of this section describes persons who are defined to be disqualified persons under the statute, including certain family members of an individual in a position to exercise substantial influence, and certain 35-percent controlled entities. Paragraph (c) of this section describes persons in a position to exercise substantial influence over the affairs of an applicable tax-exempt organization by virtue of their powers and responsibilities or certain interests they hold. Paragraph (d) of this section describes persons deemed not to be in a position to exercise substantial influence. Whether any person who is not described in paragraph (b), (c) or (d) of this section is a disqualified person with respect to a transaction for purposes of section 4958 is based on all relevant facts and circumstances, as described in paragraph (e) of this section. Paragraph (f) of this section describes special rules for affiliated organizations. Examples in paragraph (g) of this section illustrate these categories of persons.

(2) *Transition rule for lookback period.* In the case of any excess benefit transaction occurring before September 14, 2000, the lookback period described in paragraph (a)(1) of this section begins